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BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D.C. 20551

April 15, 2008

The Honorable Max Baucus
Chairman
Committee on Finance
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

This is in response to your letter of March 26, 2008, requesting that the Federal Reserve Board and Federal Reserve Bank of New York provide certain information and answers to preliminary questions regarding a financing transaction by the Federal Reserve Bank of New York in connection with the acquisition of The Bear Stearns Companies, Inc. by JPMorgan Chase & Co. The responses on behalf of the Federal Reserve to questions 1, 2, and 4 of your letter are enclosed. The New York Reserve Bank is also providing these responses separately. The responses on behalf of the Federal Reserve to the remaining questions were provided to you by letter dated April 3, 2008.

Sincerely,

Laricke Blanchard

Laricke Blanchard
Assistant to the Board

Enclosure

Federal Reserve responses to requests made by the Senate Committee on Finance by letter dated March 26, 2008, concerning the financing transaction in connection with the acquisition by JPMorgan Chase & Co. of The Bear Stearns Companies, Inc.

1. Please provide us with a memorandum of the transaction detailing all steps taken to date and steps that remain to be taken. Please include all pertinent dates.

Please see the attachment.

2. Please provide us with a memorandum describing the assets to be secured by the Federal Reserve in relation to the transaction, including, but not limited to the type of assets, face value and book value of the assets, types of mortgages underlying the assets (e.g., adjustable rate, alt-A, subprime, etc.).

The assets comprising the collateral portfolio consist largely of mortgage-related assets and their associated hedges. More specifically, the portfolio is composed of

- collateralized mortgage obligations (CMOs), the majority of which are obligations of government-sponsored entities (GSEs), such as the Federal Home Loan Mortgage Corporation ("Freddie Mac"),
- residential and commercial mortgages,
- asset-backed securities (ABS),
- commercial mortgage-backed securities (CMBS),
- various other loan obligations, and
- various hedges on the above assets.

We applied the following selection parameters:

- Only U.S. Dollar denominated assets,
- Only U.S. domiciled assets,
- Only residential and commercial mortgages that were classified "performing" as of March 14; "performing" is defined to include mortgages that are current as to principal and interest as of the last payment date plus the grace period, as documented in the servicer report, and
- Only investment grade securities, (i.e., those rated BBB- or higher by at least one of the three principal credit rating agencies and no lower than that by the others as of March 14).

As a result of the application of our selection parameters, we excluded a significant portion of the portfolio originally proposed. The following is a list of some specific assets that were excluded:

- No assets domiciled in London and Japan (ABS, CMBS, and collateralized debt/loan obligations (CDO/CLO)),
- No unrated corporate loans,
- No unrated securities,
- No residuals (e.g., equity from CDOs, ABS, CMOs).

These assets were valued by Bear Stearns as of the close of business on March 14, 2008, with a market value of $30 billion. Our asset manager (BlackRock) is currently in the process of determining the best approach to derive an independent estimate of the fair value of these assets.

4. Please provide us with copies of all documents that have been or that the parties intend to file with the U.S. Securities and Exchange Commission or any other regulatory body and any term sheets that relate to the transaction.

We have not filed and do not intend to file any documents with the SEC relating to this transaction. Additionally, please see the summary of Terms and Conditions, dated March 28, 2008, attached to our answer to question 1.

Attachment

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D.C. 20551

April 15, 2008

The Honorable Charles E. Grassley
Ranking Member
Committee on Finance
United States Senate
Washington, D.C. 20510

Dear Senator:

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Attachment

MEMORANDUM DESCRIBING STEPS TAKEN AND TO BE TAKEN BY THE FEDERAL RESERVE SYSTEM WITH RESPECT TO THE FINANCING TRANSACTION IN CONNECTION WITH THE ACQUISITION BY JPMORGAN CHASE & CO. OF THE BEAR STEARNS COMPANIES, INC.[1]

I. Steps Taken To Date with Respect to the Transaction

On the evening of Thursday, March 13, 2008, representatives from the Securities and Exchange Commission (SEC), the Board of Governors of the Federal Reserve System (Board), the Federal Reserve Bank of New York (New York Fed), and the Treasury Department took part in a conference call. On that call, the SEC staff informed the participants that the funding resources of The Bear Stearns Companies (Bear Stearns) were inadequate to meet its obligations and that the firm had concluded that it would have to file for bankruptcy protection the next morning. The SEC said it concurred in that judgment, and it would spend the evening discussing with Bear Stearns what kind of bankruptcy filing was appropriate.

The conference call that evening took place against the backdrop of an extraordinarily challenging period in the U.S. financial system. This context was critical to the decisions the Federal Reserve made over the next several days. It is important to start with an explanation of the broad risks to the economy posed by the crisis now working through the financial system.

The intensity of the crisis faced in U.S. and global financial markets is a function of the size and character of the financial boom that preceded it. This was a period of rapid financial innovation -- particularly in credit risk transfer instruments such as credit derivatives and securitized and structured products. There was considerable growth in leverage, greater reliance on ratings on structured credit products, and a marked deterioration in underwriting standards.

The innovation in financial products was accompanied by a dramatic increase in the amount of financial intermediation occurring outside the core banking system. The importance of securities broker-dealers, hedge funds, and mutual funds in the financial system rose steadily. Off-balance-sheet vehicles of various forms proliferated, and increased concentrations of longer-dated assets were held in funding vehicles with substantial liquidity risk.

The deterioration in the U.S. housing market late in the summer of 2007 precipitated a sharp rise in uncertainty about the value of securitized or structured assets. Demand for these assets contracted dramatically and the securitization market for mortgages and other credit assets stopped working. This, in turn, increased funding pressures for a diverse mix of financial institutions. Uncertainty about the magnitude and

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[1] This text is derived from testimony delivered before the Senate Committee on Banking, Housing, and Urban Affairs on April 3, 2008.

the level of losses for financial institutions fueled concern about credit risk in exposure to those institutions.

Part of the dynamic at work was that banks were forced to provide financing for -- or take over -- the assets in a range of structured investment vehicles and conduits financed by asset-backed commercial paper. As some investors attempted to liquidate their holdings of these assets, many of the traditional providers of unsecured funding to banks pulled back from their counterparties in anticipation of the potential withdrawals of funds by their own investors.

Market participants' willingness to provide term funding even against high-quality collateral declined dramatically. As a consequence, the cost of unsecured term funding rose precipitously and the volume shrunk. Banks were funding themselves at shorter and shorter maturities. As unsecured term funding markets deteriorated, the premium on liquid, marketable collateral -- such as Treasury securities -- rose considerably. Even with the dramatic actions by the Federal Reserve and other central banks to address these liquidity pressures, the strains in financial markets persisted. In many respects, conditions worsened materially in February and March. Credit spreads on financial institutions widened, equity prices declined, and market functioning deteriorated sharply. By the early part of March, the threat of a disorderly adjustment was growing.

What was being observed in U.S. and global financial markets was similar to the classic pattern in financial crises. Asset price declines -- triggered by concern about the outlook for economic performance -- led to a reduction in the willingness to bear risk and to margin calls. Borrowers needed to sell assets to meet the calls; some highly leveraged firms were unable to meet their obligations, and their counterparties responded by liquidating the collateral they held. This put downward pressure on asset prices and increased price volatility. Dealers raised margins further to compensate for heightened volatility and reduced liquidity. This, in turn, put more pressure on other leveraged investors. A self-reinforcing downward spiral of higher haircuts forced sales, lower prices, higher volatility, and still lower prices.

This dynamic poses a number of risks to the functioning of the financial system. It reduces the effectiveness of monetary policy, as the widening in spreads and risk premia worked to offset part of the reduction in the Fed Funds rate. Contagion spreads, transmitting waves of distress to other markets, from subprime to prime mortgages and even to agency mortgage-backed securities, to commercial mortgage-backed securities, and to corporate bonds and loans. In the current situation, effects were felt in the municipal and student loan markets.

The most important risk is systemic: if this dynamic continues unabated, the result would be a greater probability of widespread insolvencies, severe and protracted damage to the financial system and, ultimately, to the economy as a whole. This is not theoretical risk, and it is not something that the market can solve on its own. It carries the risk of significant damage to economic activity. Absent a forceful policy response, the consequences would be lower incomes for working families, higher borrowing costs for

housing, education, and the expenses of everyday life, lower value of retirement savings, and rising unemployment.

The Federal Reserve has taken a series of policy actions to help contain the risks to the economy posed by this financial crisis. The Federal Open Market Committee (FOMC) has reduced the nominal federal funds rate target by 300 basis points since August of 2007. Alongside these appropriately aggressive monetary actions, the Federal Reserve has taken a series of initiatives aimed at improving market liquidity and overall market functioning.

These actions are designed to allow financial intermediaries to finance with the central bank assets they can no longer finance as easily in the market. In this way these liquidity facilities reduce the need for those institutions to take the types of actions, such as selling other assets into distressed markets or withdrawing credit lines extended to other financial institutions, that would serve to amplify the pressures in markets.

In addition to these monetary policy and liquidity actions, the Federal Reserve has been working with community groups and housing advocates across the country to help homeowners navigate the complex challenges of higher resets and falling home prices. The Federal Reserve is actively working with homeowners and communities to identify solutions to avoid foreclosures and their negative effects, support appropriate consumer protection and responsible lending practices, and apply our expertise in research and evaluation to provide community groups, counseling agencies, regulators, and others with detailed analysis to support efforts to help troubled borrowers and communities.

The Federal Reserve System's response has helped reduce the risk of systemic damage to the financial system, and thereby helped mitigate a potential source of downside risk to growth. This in turn has helped mitigate the risks to the broader economy. It is important to recognize that a substantial adjustment, recognition of losses, and reduction in risk has already taken place. A range of different prices of financial assets now reflect a very cautious view of the future. The severity of the pressures in markets evident over the last few months are in part a reflection of the speed and force with which markets and institutions in our financial system adapt to fundamental changes in the outlook. This capacity to adjust and adapt is one of the great strengths of our system. Nevertheless, we still face a number of challenges ahead. The seeds of this crisis took a long time to build up, and they will take some time to work through.

With this important context, the Federal Reserve's response to the situation that arose at Bear Stearns was shaped in roughly four stages: (1) the decision on the morning of March 14 to extend a non-recourse loan through the discount window to JPMorgan Chase & Co. (JPMorgan Chase) so that JPMorgan Chase could in turn lend that money to Bear Stearns; (2) the decision on March 16 by JPMorgan Chase and Bear Stearns for JPMorgan Chase to acquire Bear Stearns and guarantee certain of its liabilities, along with an agreement in principle that the New York Fed would provide certain financing in the context of that acquisition; (3) the launching of the Primary Dealer Credit Facility; and (4) the events of the following week, culminating in the March 24 announcement of

revised merger agreement and guaranty terms between JPMorgan Chase and Bear Stearns, and the finalizing of the terms and structure of the associated loan from the New York Fed.

With regard to the market situation in which Bear Stearns was operating in the days leading up to March 13, fixed income traders had begun hearing rumors that European financial institutions had stopped doing fixed income trades with Bear Stearns. Fearing that their funds might be frozen if Bear Stearns wound up in bankruptcy, a number of U.S.-based fixed-income and stock traders that had been actively involved with Bear Stearns had reportedly decided to halt such involvement. Many firms started pulling back from doing business with Bear Stearns. Some hedge funds that had used Bear Stearns to borrow money and clear trades were withdrawing cash from their accounts. Some large investment banks stopped accepting trades that would expose them to Bear Stearns, and some money market funds reduced their holdings of short-term Bear Stearns-issued debt. The rumors of Bear Stearns' failing financial health caused its balance of unencumbered liquidity on March 13 to decline sharply to levels that were not adequate to cover maturing obligations and funds that could be withdrawn freely. This precipitated the phone call with representatives of the Federal Reserve, the SEC, and the Treasury on the evening of March 13.

The news that Bear Stearns' liquidity position was so dire that a bankruptcy filing was imminent presented a very difficult set of policy judgments. In our financial system, the market sorts out which companies survive and which fail. However, under the circumstances prevailing in the markets the issues raised in this specific instance extended well beyond the fate of one company. It became clear that Bear Stearns' involvement in the complex and intricate web of relationships that characterize our financial system, at a point in time when markets were especially vulnerable, was such that a sudden failure would likely lead to a chaotic unwinding of positions in already damaged markets. Moreover, a failure by Bear Stearns to meet its obligations would have cast a cloud of doubt on the financial position of other institutions whose business models bore some superficial similarity to Bear Stearns', without due regard for the fundamental soundness of those firms.

The sudden discovery by Bear Stearns' derivatives counterparties that important financial positions they had put in place to protect themselves from financial risk were no longer operative would have triggered substantial further dislocation in markets. This would have precipitated a rush by Bear Stearns' counterparties to liquidate the collateral they held against those positions and to attempt to replicate those positions in already very fragile markets.

In short, a sudden, disorderly failure of Bear Stearns would have brought with it unpredictable but severe consequences for the functioning of the broader financial system and the broader economy, with lower equity prices, further downward pressure on home values, and less access to credit for companies and households.

Following that initial call with the SEC on March 13, staff at the Federal Reserve in New York and in Washington spent the night focusing on the implications of a large-scale default by Bear Stearns and how the consequential damage might be contained. Bear Stearns renewed conversations that began earlier that day with JPMorgan Chase, which is Bear's clearing bank for its repo arrangements, to explore a range of possible financing options. The New York Fed dispatched a team of examiners to Bear Stearns to look at its books so that the Federal Reserve could get a better handle on what could be done. The Federal Reserve gathered the best information it could, evaluated the risks involved, and explored a range of possible actions.

At 5:00 a.m., representatives of the Board, the New York Fed, and the Treasury took part in a conference call to review the options and decide on the way forward. After careful deliberation, together the participants decided on a course of action that would at least buy some time to explore options to mitigate the foreseeable damage to the financial system. With the support of the Secretary of the Treasury, Chairman Bernanke and the Board of Governors agreed that the New York Fed would extend an overnight non-recourse loan through the discount window to JPMorgan Chase, so that JPMorgan Chase could then "on-lend" that money to Bear Stearns.

This action was designed to allow the parties to get to the weekend, and to enable them to pursue work along two tracks: first, for Bear Stearns to continue to explore options with other financial institutions that might enable it to avoid bankruptcy; and second, for policymakers to continue the work begun on Thursday night to try to contain the risk to financial markets in the event no private-sector solution proved possible.

Over the course of that day, March 14, Bear Stearns was downgraded by the credit rating agencies, and the flight of customer business from Bear Stearns accelerated. This set in motion a chain of decisions across the financial system as market participants prepared for the possibility that Bear Stearns would not be open for business once Asian markets opened on Sunday night. This highlighted the urgency of working toward a solution over the weekend, ideally a solution that would definitively address the prospect of default by Bear Stearns.

Bear Stearns approached several major financial institutions, beginning on March 13. Those discussions intensified on Friday and Saturday. Bear Stearns' management provided the Federal Reserve with periodic progress reports about a possible merger. Although several different institutions expressed interest in acquiring all or part of Bear Stearns, it was clear that the size of Bear Stearns, the apparent risk in its balance sheet, and the limited amount of time available for a possible acquirer to conduct due diligence compounded the difficulty. Ultimately, only JPMorgan Chase was willing to consider an offer of a binding commitment to acquire the firm and to stand behind Bear's substantial short-term obligations.

As JPMorgan Chase and other institutions conducted due diligence, staff of the Federal Reserve in New York and Washington continued to examine ways to contain the effects of a default by Bear Stearns. As part of these discussions, the Federal Reserve

began to design a new facility that would build on other liquidity initiatives taken by the Federal Reserve System, and provide a more powerful form of liquidity to major financial institutions.

Following the announcement on March 11 of the Term Securities Lending Facility, which allowed primary dealers to pledge a wider range of collateral in order to borrow Treasury securities, the Federal Reserve had consulted with market participants on how to structure the auctions to maximize their potential benefits to market functioning. Those discussions yielded a number of helpful suggestions. In view of those suggestions, and after considering the greater risks to the financial system posed by the Bear Stearns situation, the Federal Reserve was able to work quickly on a companion facility that would transmit liquidity to parts of the market where it could be most powerful.

This is what led the Board to approve the establishment of the Primary Dealer Credit Facility on March 16. Under Section 13(3) of the Federal Reserve Act, the Board is empowered to authorize a Federal Reserve Bank like the New York Fed to lend to a corporation, such as an investment bank, in extraordinary circumstances under which there is evidence that the corporation cannot "secure adequate credit accommodations from other banking institutions." The Board needed to make the statutory finding that the circumstances were exigent and extraordinary, and it did so, based on the situation prevailing in the financial markets and the distinct possibility that absent an assurance of liquidity to major investment banks the deterioration in financial conditions likely would have continued with substantial effects on the economy.

On Sunday morning, executives at JPMorgan Chase informed us that they had become significantly more concerned about the scale of the risk that Bear Stearns and its many affiliates had assumed. They were also concerned about the ability of JPMorgan Chase to absorb some of Bear Stearns' trading portfolio, particularly given the uncertainty ahead about the ultimate scale of losses facing the financial system. In this context, the Federal Reserve began to explore ways in which we could help facilitate a more orderly solution to the Bear Stearns situation. The Federal Reserve did not have the authority to acquire an equity interest in either Bear Stearns or JPMorgan Chase, nor were we prepared to guarantee Bear Stearns' very substantial obligations. The only feasible option for buying time would have required open-ended financing by the Federal Reserve to Bear Stearns into an accelerating withdrawal by Bear' Stearns' customers and counterparties.

We did, however, have the ability to lend against collateral, as in the back-to-back non-recourse arrangement that carried Bear Stearns into the weekend. After extensive discussion between Chairman Bernanke, President Geithner of the New York Fed, and Secretary Paulson, and with their full support, the New York Fed and JPMorgan Chase reached an agreement in principle that the New York Fed would assist with non-recourse financing. Using section 13(3) of the Federal Reserve Act, with the approval of the Board, the New York Fed on March 16 agreed in principle to lend $30 billion to JPMorgan Chase and to secure the lending with a pledge of Bear Stearns assets valued by

Bear Stearns on March 14 at approximately $30 billion. This step made it possible for JPMorgan Chase to agree to acquire Bear Stearns and to step in immediately to guarantee all of Bear Stearns' short-term obligations. This guarantee was especially important to stave off the feared systemic effects that would be triggered by the panic of a Bear Stearns bankruptcy filing and of the failure to honor its obligations. Agreeing to lend against a portfolio of securities reduced the risk that those assets would be liquidated quickly, exacerbating already fragile conditions in markets.

On the evening of Sunday the 16th, President Geithner sent a letter to James Dimon, the CEO of JPMorgan Chase, to memorialize the fact that a preliminary agreement had been reached that the New York Fed would assist the acquisition with $30 billion in financing, with the understanding that the parties would continue working during the week towards a formal contract. The Federal Reserve also provided regulatory approvals, including under section 23A of the Federal Reserve Act, to assist with the merger and a transitional period for phasing in the assets under our capital rules.

The announcement of the agreement between Bear Stearns and JPMorgan Chase and the announcement of the Primary Dealer Credit Facility were finalized just before Asian markets opened on Sunday night, and the announcement of these actions helped avert the damage that would have accompanied default.

On Monday morning, March 17, the approximately $13 billion back-to-back non-recourse loan through JPMorgan Chase to Bear Stearns was repaid to the Fed, with weekend interest of nearly $4 million. The Primary Dealer Credit Facility was made available to the market. And at the request of and with the full cooperation of the SEC, examiners from the New York Fed were sent into the major investment banks to give the Federal Reserve the direct capacity to assess the financial condition of these institutions.

Discussions were also continuing regarding the details of the Federal Reserve's financial arrangement with JPMorgan Chase. The legal teams engaged in the meticulous work of finalizing the legal structure of the lending arrangement that had been agreed to in principle, including defining the precise pool of collateral and related hedges that would secure the $30 billion loan.

At the same time, several infirmities became evident in the agreement between JPMorgan Chase and Bear Stearns during the week of March 17th that needed to be cured.

Negotiations between the two sets of counterparties proceeded almost immediately between the New York Fed and JPMorgan Chase on the one hand, and between JPMorgan Chase and Bear Stearns on the other. The New York Fed and JPMorgan Chase discussed the details for the secured financing. Bear Stearns and JPMorgan Chase continued to negotiate changes to the merger agreement that would tighten the guarantee and provide the necessary certainty that the merger would be consummated. All the parties shared an overriding common interest: to move toward a successful merger and avoid the situation in which they found themselves on March 14.

The extended Easter weekend saw intense sets of bilateral negotiations among the three parties. The deal, finally struck in the early morning hours on March 24, held benefits for all parties. That deal included a new, more precise guaranty from JPMorgan Chase, which lifted the cloud of default risk that had been hanging over the transaction. Bear Stearns stockholders were to receive a higher share price. In addition to fixing the guaranty, JPMorgan Chase gained assurance that its merger with Bear Stearns would take place. The New York Fed obtained significant downside protection on the loan and a tighter guaranty on its exposure. The new Federal Reserve financing facility will be in place for a maximum of ten years, though it could be repaid earlier, at the discretion of the Federal Reserve. This is an important feature: the assets that are being pledged as collateral can be managed on a long-term basis so as to minimize the risks to the market and the risk of loss. They can be held or disposed of at any time over the next decade.

In keeping with the traditional role of a lender of last resort, the extensions of credit to Bear Stearns that the Federal Reserve made to facilitate the merger were secured by collateral. The $29 billion loan will be extended only when and if JPMorgan Chase and Bear Stearns merge. The Federal Reserve will be protected from loss by three different risk mitigants: first, a substantial pool of professionally-managed collateral that, as of March 14, was valued at $30 billion; second, the agreement on the part of JPMorgan Chase to absorb the first $1 billion of any loss that ultimately occurs in connection with this arrangement; and third -- and perhaps most importantly -- a long-term horizon during which the collateral will be safe-kept and, if sold, will be sold in an orderly fashion that is not affected by the unnaturally strong downward market pressures that have been associated with the recent liquidity crisis.

On April 1, the Board approved under the Bank Holding Company Act the proposal by JPMorgan Chase to acquire Bear Stearns Bank & Trust, a Bear Stearns subsidiary.

II. Steps To Be Taken with Respect to the Transaction.

Assuming that the JPMorgan Chase/Bear Stearns merger takes place, several administrative actions must be taken to implement the Federal Reserve financing transaction described in the following Summary of Terms and Conditions relating to the transaction, dated March 28, 2008. A Delaware limited liability company and two common law trusts, which will, directly or indirectly, hold the collateral and associated hedges for the loan, must be organized. The parties to the transaction must execute and deliver satisfactory loan and security and other documentation and various corporate organizational steps must be completed. The terms of the contract between the New York Fed and the asset manager, BlackRock Financial Management, Inc., which will manage the collateral pool relating to the loan, must be finalized. Required opinions relating to specific parts of the transaction must be provided by the parties.

EXECUTION COPY

Summary of Terms and Conditions

March 28, 2008

Concurrently with, and subject to the consummation of the merger (the "Merger") in all material respects on the terms described in the Agreement and Plan of Merger, dated as of March 16, 2008 (as amended, the "Merger Agreement"), between The Bear Stearns Companies Inc. ("Bear Stearns") and JPMorgan Chase & Co., a newly formed Delaware limited liability company (the "Borrower") will enter into an agreement with Bear Stearns and/or certain of its subsidiaries and/or affiliates (collectively, the "Seller") pursuant to which the Borrower will acquire (whether directly or through participations) the Portfolio (as defined below) and the Pre-Closing Date Proceeds Amount (as defined below) from the Seller pursuant to an asset acquisition agreement (the "Asset Acquisition Agreement") in consideration of the payment of a cash Purchase Price (as defined below) and the assumption of certain liabilities, the source of the funding of which shall be the proceeds of (a) borrowings under a Tranche A senior secured loan facility (the "Tranche A Loan Facility") provided by the Federal Reserve Bank of New York (the "NY Fed") in an aggregate principal amount, not to exceed $29,000,000,000, equal to the Purchase Price plus the par value of the Unfunded Forward Commitments (as defined below) less $1,000,000,000 and (b) borrowings under a Tranche B subordinated secured loan facility (the "Tranche B Loan Facility" and, together with the Tranche A Loan Facility, the "Loan Facilities") provided by JPMorgan Chase Bank, N.A (the "JPMC") in an aggregate principal amount equal to $1 billion. In addition, the NY Fed will be entitled to a residual interest in the Portfolio (such interest, the "Residual Interest"). Set forth below is a summary of the terms and conditions for the Loan Facilities.

1. PARTIES

Borrower:	The Borrower (as defined above).
Administrative Agent, Collateral Agent and Depositary Bank:	An entity (or entities) to be determined by the NY Fed (in such capacities, the "Agent").
Tranche A Lender:	The NY Fed (the "Tranche A Lender").
Tranche B Lender:	JPMC (the "Tranche B Lender" and, together with the Tranche A Lender, the "Lenders").
Asset Manager:	Blackrock Financial Management, Inc. and its affiliates (in such capacity, the "Asset Manager"). The Asset Manager will be solely the agent of the NY Fed, but will owe the other Secured Parties (as defined below) and the Borrower a duty of good faith and fair dealing. The Asset Manager shall be paid fees as determined by the NY Fed and notified to JPMC.

2. DESCRIPTION OF ASSET ACQUISITION AGREEMENT

Seller:	The Seller.
Buyer:	The Borrower.

Asset Acquisition Agreement: Pursuant to the Asset Acquisition Agreement, the Seller will sell to the Buyer (whether directly or through participations) without recourse (but subject to, and with full recourse for the breach of, representations and warranties relating to good title and authority to transfer) the assets identified by JPMC, the NY Fed and the Asset Manager as described on Schedule A hereto (the "Scheduled Collateral Pool"), together with the hedges identified by JPMC, the NY Fed and the Asset Manager as described on Schedule B hereto (the "Related Hedges") and including the Pre-Closing Date Proceeds Amount. For the avoidance of doubt, the Related Hedges include the amount that the Borrower would have to pay to, or the amount that the Borrower would receive from, the applicable counterparty if the Borrower had entered into an identical transaction on March 14, 2008 based on the Bear Stearns marks as of such date (the "Transfer Value"), as well as all accumulated mark to market gains or losses thereafter and any cash proceeds as a result of Related Hedges' being unwound.

Purchase Price: The purchase price (the "Purchase Price") for the Scheduled Collateral Pool and the Related Hedges (including the Pre-Closing Date Proceeds Amount) is an amount, not to exceed $30 billion, determined as provided in "Pricing of the Scheduled Collateral Pool and Related Hedges" below minus the par value of the total unfunded forward commitments, whether contingent or non-contingent (the "Unfunded Forward Commitments") included in the Scheduled Collateral Pool.

Seller Payment: On the Closing Date, the Seller will pay (the "Seller Payment") to the Borrower, in consideration of the Borrower's assumption of the Seller's liabilities under the Unfunded Forward Commitments, an amount equal to the difference (if positive) between (x) the par value of such commitments and (y) the market value of such commitments as of March 14, 2008 or, if such market value is unavailable, the market value shall be determined by reference to the market value of the related funded portion of any such commitment as of March 14, 2008, but, if no related funded portion exists and there is otherwise no market value associated with such commitment, the market value shall be determined based on "haircuts" to par as shall be mutually agreed between the NY Fed, JPMC and the Asset Manager. Such amount will be deposited into the Reserve Account.

Related Hedges: As of the Closing Date, the Borrower will assume as an economic matter the obligations under the Related Hedges and receive the benefits thereof by entering into a total return swap with the Seller, such total return swap having an initial fair value as of the Closing Date equal to the fair value of the Related Hedges as of the Closing Date. The Controlling Party (as defined below) shall have the right to make all

determinations related to the underlying hedges (e.g., whether and when to terminate) that are subject to the total return swap. At the request of the NY Fed, the Seller will use its commercially reasonable efforts to replace the total return swap with direct hedges with underlying counterparties through novation.

Guaranty: JPMC will irrevocably and unconditionally guaranty the obligations of the Seller under the Asset Acquisition Agreement and the total return swap.

3. AGREEMENTS IN EFFECT PRIOR TO THE CLOSING DATE

Pricing of the Scheduled Collateral Pool and Related Hedges: The price of the Scheduled Collateral Pool shall equal the sum of (i) the value of such collateral pool on the books of the Seller as of March 14, 2008 (including with respect to the assumption of liabilities for Unfunded Forward Commitments), irrespective of any mark-downs or mark-ups in such collateral after March 14, 2008 and irrespective of when such collateral pool is actually pledged to secure the Loan Facilities and (ii) the Transfer Value of the Related Hedges.

Management of Scheduled Collateral Pool and Related Hedges: Prior to the Closing Date and upon final determination of each particular asset or hedge comprising a part of the Scheduled Collateral Pool or the Related Hedges, JPMC will delegate management rights with respect to such assets or hedges to the NY Fed which in turn will delegate such rights to the Asset Manager, and the NY Fed and the Asset Manager will have the right to liquidate assets in the Scheduled Collateral Pool and Related Hedges or both in their discretion at any time.

Pre-Closing Date Proceeds Amount: On the Closing Date, the Pre-Closing Date Proceeds Amount (to the extent such amount is positive) will be deposited into the Reserve Account.

The "Pre-Closing Date Proceeds Amount" means an amount, determined as of the Closing Date, equal to the sum (without duplication) of the following amounts paid or received in respect of the assets and liabilities in the Portfolio during the period from March 14, 2008 to the Closing Date:

(i) the cash proceeds from the sale of assets comprising a portion of the Scheduled Collateral Pool; plus

(ii) all amounts received from the amortization or prepayment of principal on any assets comprising a portion of the Scheduled Collateral Pool; plus

(iii) the interest payments on the Scheduled Collateral Pool; plus

(iv) all periodic, termination and other payments (excluding the

posting of margin) received from counterparties on the Related Hedges; minus

(v) all periodic, termination and other payments (excluding the posting of margin) made to counterparties on the Related Hedges; minus

(vi) allocated funding costs (at the Primary Credit Rate (as defined below)).

It is understood that prior to the Closing Date, the NY Fed has no responsibility to provide any margin or other credit support for any hedge.

Guaranty: JPMC will enter into, and keep in full force and effect, the Guarantee, dated as of March 23, 2008, in favor of the NY Fed.

NY Fed Commitment: The NY Fed commits to provide the financing described herein in connection with JPMC's acquisition of Bear Stearns to address the extraordinary circumstances in the market on March 14, 2008 and the surrounding days. The NY Fed has not committed to make a similar facility to any other party or under any different circumstances.

Confidentiality: The transactions contemplated by this Summary of Terms and Conditions and all other materials, information, documents and discussions regarding this Summary of Terms and Conditions and the transactions contemplated hereby shall be kept confidential by JPMC.

4. <u>TYPES AND AMOUNTS OF LOAN FACILITIES</u>

<u>Loan Facilities</u> The Lenders hereby agree to provide financing to the Borrower as follows:

Type and Amount: Loan Facilities (the loans thereunder, the "<u>Loans</u>") as follows:

<u>Tranche A Loan Facility</u>: A ten-year term loan facility (subject to extension as provided below) provided by the Tranche A Lender to the Borrower in a principal amount equal to the Purchase Price plus the par value of the Unfunded Forward Commitments minus $1,000,000,000, but in any case not to exceed $29,000,000,000 (the loan thereunder, the "<u>Tranche A Loan</u>"). The Tranche A Loan shall be repayable or be terminated in the manner described under the section below entitled "<u>Cash Flow Waterfall</u>".

<u>Tranche B Loan Facility</u>: A ten-year term loan facility (subject to extension as provided below) provided by the Tranche B Lender to the Borrower in a principal amount of $1,000,000,000 (the loan thereunder, the "<u>Tranche B Loan</u>"). The Tranche B

Loan will be subordinate in right of payment to the Tranche A Loan and shall be repayable or be terminated in the manner described under the section below entitled "Cash Flow Waterfall".

Availability: The Loans shall be made in a single drawing on the Closing Date (as defined below).

Maturity Date: The Loans will mature on the tenth anniversary of the Closing Date; *provided* that the NY Fed may in its sole discretion at any time and from time to time extend the maturity date of either or both of the Loan Facilities; *provided, further*, that the NY Fed may not extend the maturity date of the Tranche B Loan after the Tranche A Loan is paid in full or to a maturity date later than the maturity date of the Tranche A Loan without the consent of the Tranche B Lender.

Purpose: The proceeds of the Loans shall be used to finance the acquisition of the Portfolio and the Pre-Closing Date Proceeds Amount from the Seller and to fund the Delayed Draw Account (as defined below).

5. INTEREST PAYMENT PROVISIONS

Interest Rates: The Tranche A Loans shall bear interest at a rate per annum equal to the Primary Credit Rate in effect from time to time.

The Tranche B Loans shall bear interest at a rate per annum equal to the Primary Credit Rate plus 450 bps in effect from time to time.

As used herein, the "Primary Credit Rate" means the discount rate charged by the NY Fed for loans under its primary credit program from time to time in effect.

Interest Payment Dates: Interest shall accrue and be compounded on a quarterly basis and be payable on payment dates as set forth under the section below entitled "Cash Flow Waterfall".

6. COLLATERAL, RESERVE ACCOUNT AND DELAYED DRAW ACCOUNT

Collateral: The obligations of the Borrower in respect of the Loan Facilities and the hedge agreements entered into by the Borrower shall be secured by a first priority perfected security interest in (a) all of its assets including the Scheduled Collateral Pool and the Related Hedges (collectively, the "Portfolio"), (b) the Reserve Account (as defined below) and related investments, (c) the Delayed Draw Account and related investments and (d) all proceeds of the foregoing (collectively, the "Collateral"). The

Lenders and the counterparties under the hedge agreements shall collectively be referred to herein as the "Secured Parties".

All of the above described security interests will be created on terms, and pursuant to documentation (including custody and control agreements), satisfactory to the NY Fed, and none of the Collateral will be subject to any other pledges, liens or security interests.

Reserve Account:	On the Closing Date, the Pre-Closing Date Proceeds Amount (to the extent such amount is positive) and the proceeds of the Seller Payment, if any, will be deposited into the Reserve Account. On and after the Closing Date, all cash flow generated by the Collateral and any other income or proceeds earned or received by the Borrower shall be deposited with the Agent and credited to a reserve account (the "Reserve Account") and held in such Reserve Account for the benefit of the Secured Parties pending distribution to the Secured Parties in accordance with the Cash Flow Waterfall as hereinafter provided. Notwithstanding the foregoing, except to the extent funds are required to make a Seller Distribution (as defined below) or to pay any Operating Expenses that were accrued on or prior to the Closing Date and remain unpaid, amounts on deposit in the Reserve Account may not be distributed (other than in respect of payments required under the hedge agreements) to the extent that the amount on deposit therein will be less than the Unfunded Swap Exposure (the "Minimum Balance Requirement"). "Unfunded Swap Exposure" means the maximum total liability of the Borrower under all hedge agreements minus all amounts posted as collateral to the related hedge counterparties. Amounts on deposit in the Reserve Account shall be invested in certain eligible investments at the discretion of the Controlling Party (as defined below). Subject to the Minimum Balance Requirement, the Controlling Party (and its agents, including the Asset Manager) shall control in its sole discretion all decisions regarding the Collateral, the proceeds on deposit in the Reserve Account and decisions as to timing and amounts of distributions from the Reserve Account.
Delayed Draw Account:	On the Closing Date, a portion of the proceeds from the Loans equal to the amount of Unfunded Forward Commitments shall be deposited with the Agent and credited to a delayed draw account (the "Delayed Draw Account"). Amounts on deposit in the Delayed Draw Account shall be withdrawn from time to time by the Agent in order to satisfy any payment obligations of the Borrower in respect of any such

commitments when and as such obligations become due.

Amounts on deposit in the Delayed Draw Account shall be invested in certain eligible investments at the discretion of the Controlling Party (as defined below).

To the extent any such Unfunded Forward Commitments expire or amounts remain on deposit in the Delayed Draw Account in excess of any remaining Unfunded Forward Commitments, the Agent shall transfer such amounts from the Delayed Draw Account to the Reserve Account.

7. CASH FLOW WATERFALL

Funds in the Reserve Account shall be paid on any business day as determined by the Controlling Party in its sole discretion in the following order of priority, subject, except as set forth in the last paragraph of "Waterfall Priority", to the Minimum Balance Requirement:

Waterfall Priority:

(a) First, to pay Operating Expenses that are then due and payable.

"Operating Expenses" mean all costs and expenses of administering the Portfolio, the Reserve Account, the other Collateral, the Loan Facilities and Loan Documentation (as defined below) and the Borrower, including all fixed fees and expenses of the Asset Manager and the Agent, all legal, accounting and other professional fees and expenses and other administrative costs and expenses of the Borrower, all legal, accounting and other professional fees and expenses and other administrative costs and expenses (other than those of the Tranche B Lender, the Seller or any of their respective advisors or agents) associated with the negotiation, preparation, execution and delivery of this term sheet and the Loan Documentation (as defined below) and with the administration of the Loan Documentation and any amendment or waiver or enforcement action with respect thereto (including the fees, disbursements and other charges of counsel), taxes that are determined to be payable from time to time, all amounts payable in respect of hedges (including, without limitation, periodic payments and termination payments), the costs of entering into any additional hedges as may be determined to be necessary or appropriate by the Controlling Party and any indemnity claims.

(b) Second, beginning on or after the second anniversary of the Closing Date or such earlier date as shall be determined by the Controlling Party (the period from the Closing Date until the second anniversary of the Closing Date or such earlier date the "Accumulation Period"), to pay all or any portion of the

outstanding principal amount of the Tranche A Loan Facility; *provided* that, if the Controlling Party elects to pay any of the outstanding principal amount of the Tranche A Loan Facility prior to the second anniversary of the Closing Date, the full outstanding principal amount of the Tranche B Loan Facility, together with all accrued and unpaid interest thereon, shall be simultaneously repaid.

(c) Third, after the Accumulation Period, but so long as the entire outstanding principal amount of the Tranche A Loan Facility has been repaid in full, to pay all or any portion of the accrued but unpaid interest outstanding under the Tranche A Loan Facility.

(d) Fourth, after the Accumulation Period, but so long as the entire outstanding principal amount, all accrued and unpaid interest and all other outstanding amounts, in each case under the Tranche A Loan Facility have been repaid in full, to pay all or any portion of the outstanding principal amount of the Tranche B Loan Facility.

(e) Fifth, after the Accumulation Period, but so long as the entire outstanding principal amount, all accrued and unpaid interest and all other outstanding amounts, in each case under the Tranche A Loan Facility have been paid in full and so long as the entire outstanding principal amount of the Tranche B Loan Facility has been repaid in full, to pay all or any portion of the accrued but unpaid interest outstanding under the Tranche B Loan Facility.

(f) Sixth, after the Accumulation Period, but so long as the entire outstanding principal amount, all accrued and unpaid interest and all other outstanding amounts, in each case under both the Tranche A Loan Facility and the Tranche B Loan Facility have been paid in full, all hedges have been terminated and all amounts payable under the hedges have been paid in full, to pay any fees and expenses or other amounts owing to the extent not constituting Operating Expenses.

(g) Seventh, after the Accumulation Period, but so long as the entire outstanding principal amount, all accrued and unpaid interest and all other outstanding amounts, in each case under both the Tranche A Loan Facility and the Tranche B Loan Facility have been paid in full, all hedges have been terminated and all amounts payable under the hedges have been paid in full, and any fees and expenses or other amounts owing to the extent not constituting Operating Expenses have been paid in full, to pay all remaining amounts to the NY Fed as holder of the Residual Interest.

Notwithstanding the foregoing on any business day (including the Closing Date) as determined in the sole discretion by the Controlling Party, (i) to the extent that the Pre-Closing Date Proceeds Amount is negative, funds in the Reserve Account shall be withdrawn, from time to time if necessary, to make a payment or payments to the Seller in an amount equal to the absolute value of the Pre-Closing Date Proceeds Amount (the "Seller Distribution") and (ii) after giving effect to all payments required by clause (i), funds in the Reserve Account shall be withdrawn, from time to time if necessary, and used to pay all Operating Expenses that accrued on or prior to the Closing Date and remain unpaid.

Once prepaid, Loans may not be reborrowed.

Termination: Regardless of whether any amounts remain outstanding thereunder, each of the Loan Facilities and the Residual Interest shall be terminated on the date on which the entire Portfolio has been fully liquidated and all proceeds thereof, including all amounts on deposit in the Reserve Account and the Delayed Draw Account, have been distributed in the manner set forth above.

8. CERTAIN CONDITIONS

Initial Conditions: The availability of the Loan Facilities shall be conditioned upon the satisfaction of the following conditions (the date upon which all such conditions precedent shall be satisfied, the "Closing Date"): the execution and delivery by the Agent, the Lenders, the Borrower and the Asset Manager of Loan Documentation satisfactory to the NY Fed, the closing of the Merger in all material respects on the terms set forth in the Merger Agreement, the consummation of the sale of the Portfolio (including the Pre-Closing Date Proceeds Amount) on the terms set forth in the Asset Acquisition Agreement and the creation and perfection of security interests in the Collateral pursuant to arrangements satisfactory to the NY Fed.

9. CERTAIN DOCUMENTATION MATTERS

The documentation for the Facilities (the "Loan Documentation") shall contain representations, warranties, covenants and events of default (in each case, applicable to the Borrower) customary for financings involving special, limited purpose borrowers and with other terms deemed appropriate by the NY Fed.

Voting and Control: The NY Fed shall be the "Controlling Party" on and after the Closing Date and shall be permitted to make all decisions regarding the Collateral, the Reserve Account, the Delayed Draw Account and the Loan Documentation, including the timing and amounts of distributions and whether or not a default

or event of default has occurred and whether or not to begin the exercise of remedies.

In addition the Controlling Party will have complete discretion with respect to all decisions regarding the management of the Collateral (which it may elect to delegate to the Asset Manager), including decisions as to when to liquidate Collateral and as to when or if to terminate hedges or enter into hedges. In exercising such control the Controlling Party and its agents shall have no duty to maximize returns on the Collateral or to take into account the interests of the Tranche B Lender.

Notwithstanding the foregoing, the consent of (i) each Lender directly affected thereby shall be required with respect to (a) reductions in the outstanding principal amount of any Loan (except as otherwise expressly permitted above) and (b) any amendment to the Loan Documentation or any other transaction document that is materially adverse to such Lender and (ii) each Secured Party directly affected thereby shall be required with respect to any materially adverse change in such Secured Party's position in the cash flow waterfall.

Assignments and Participations:	The Tranche B Lender shall not be permitted to assign all or a portion of its Tranche B Loan or sell participations in its Tranche B Loan except to its affiliates.
Indemnification and Exculpation:	The Agent, the Asset Manager, the Controlling Party and the Lenders (and their affiliates and their respective officers, directors, employees, advisors and agents) will have no liability for, and will be indemnified by the Borrower and held harmless against, any losses, claims, damages, liabilities or expenses (collectively, "Liabilities") incurred in respect of, or arising out of, or in connection with, the financing contemplated hereby (including in connection with the management of the Portfolio and other Collateral) or the use or the proposed use of proceeds thereof, except to the extent they are found by a final, non-appealable judgment of a court of competent jurisdiction to arise from the gross negligence, bad faith or willful misconduct of such person.

Each Secured Party agrees not to assert or claim that the Agent, the Asset Manager, the Controlling Party or any other Secured Party (and their affiliates and their respective officers, directors, employees, advisors and agents) has any liability for any Liabilities incurred in respect of, or arising out of, or in connection with, the financing contemplated hereby (including in connection with the management of the Portfolio and other Collateral) or the use or the proposed use of proceeds thereof, except to the extent they are found by a final, non-appealable judgment of a court of competent jurisdiction to arise from the gross negligence, bad faith or willful misconduct of such

person.

Governing Law and Forum: State of New York.

Accepted and agreed to as of
March 28, 2008:

This Summary of Terms and Conditions may be executed in counterparts.

THE FEDERAL RESERVE BANK OF NEW YORK

By: ______________________

Name: Timothy F. Geithner

Title: President

JPMORGAN CHASE & CO.

By: ______________________

Name:

Title:

Accepted and agreed to as of
March 28, 2008:

This Summary of Terms and Conditions may be executed in counterparts.

THE FEDERAL RESERVE BANK OF NEW YORK

By: ____________________
Name:
Title:

JPMORGAN CHASE & CO.

By: ____________________
Name: James Dimon
Title: Chairman and Chief Executive Officer

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Report Pursuant to Section 129 of the Emergency Economic Stabilization Act of 2008: Bridge Loan to The Bear Stearns Companies Inc. Through JPMorgan Chase Bank, N.A.

Overview

On Friday, March 14, 2008. the Board of Governors of the Federal Reserve System (Board), by the unanimous vote of all available members, authorized under section 13(3) of the Federal Reserve Act (12 U.S.C. § 343) the Federal Reserve Bank of New York (FRBNY) to extend credit to The Bear Stearns Companies, Inc, (Bear Stearns) through JPMorgan Chase Bank, N.A. (JPMC Bank).[1] The extension of credit was designed to provide funding to Bear Stearns to meet its immediate liquidity needs for that day and to give the company and policymakers additional time to develop a more permanent solution to the company's severe liquidity pressures that threatened to cause its sudden default and bankruptcy.

Background and Details on the Extension of Credit to Bear Stearns Through JPMC Bank

In March 2008, Bear Stearns was one of the largest securities firms in the country. As of February 29, 2008, Bear Stearns reported total consolidated assets of approximately $399 billion. Bear Stearns engaged in a broad range of activities, including investment banking, securities and derivatives trading and clearing, brokerage services, and originating and securitizing commercial and residential mortgage loans. As a result of these

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[1] Section 13(3), which relates to discounts to individuals, partnerships, and corporations, generally requires an affirmative vote of at least five members of the Board to approve an extension of credit under that provision. One member of the Board was unavailable at the time of the Board vote because he was enroute to the Board from Helsinki, Finland. As permitted under section 11(r)(2) of the Federal Reserve Act (12 U.S.C. § 248(r)(2)), however, the Board's action approving the March 14 extension of credit to Bear Stearns was adopted by the unanimous vote of all available Board members. The approval of the credit by less than five Board members complied with all of the requirements of section 11(r)(2) for taking such action. The available members of the Board then in office unanimously approved the action and, among other things, determined that action on the extension of credit was required before the other member of the Board required to vote on the matter could be available to participate by any available means. As required by section 11(r)(2), the Board submitted a record of its action approving the credit extension to the Chairmen of the appropriate Congressional committees.

activities, Bear Stearns maintained a large portfolio of mortgage-related securities and other debt instruments. Like most large securities firms, the company heavily financed itself in the short-term securities repurchase market.

Financial conditions deteriorated markedly between mid-January and mid-March 2008. Volatility was steadily increasing and liquidity was quickly declining in many credit markets – including in particular the market for residential mortgage-backed securities, but also in the markets for other asset-backed securities, corporate securities, and municipal securities. Moreover, many market participants were financing a large portion of their holdings of these long-term securities in short-term collateralized funding markets.

The senior management of Bear Stearns notified the Federal Reserve on the evening of Thursday, March 13, that it anticipated that many of its counterparties would on Friday not agree to roll over their repurchase agreements and, therefore, that Bear Stearns would be required on Friday to repay a significant portion of its repurchase agreement liabilities. Bear Stearns expected that it would not have sufficient funds or liquid assets to repay these obligations as they came due and would not be able during the short period before the markets opened on Friday to find a private-sector source of alternative financing. Bear Stearns reported that it would likely have to file for bankruptcy protection on Friday unless the Federal Reserve were willing to provide Bear Stearns with liquidity.

The sudden imminence of insolvency for Bear Stearns, the large presence of Bear Stearns in several important financial markets (including in particular the markets for repo-style transactions, over-the-counter derivative and foreign exchange transactions, mortgage-backed securities, and securities clearing services), and the potential for contagion to similarly situated firms raised significant concern that financial markets would be seriously disrupted if Bear Stearns were suddenly unable to meet its obligations to counterparties. Most crucially, the consequences of an unexpected and disorderly default or insolvency by Bear Stearns – a major borrower and lender in the repurchase agreement market – could have seriously disrupted this very large, important, and increasingly strained market for short-term secured financing. Market participants were likely to respond to the failure of Bear Stearns by withdrawing generally from short-term collateralized funding markets, resulting in a dramatic drop in the

overall availability of short-term financing, and threats to the liquidity and possibly the solvency of other large and highly leveraged financial institutions.

To address the imminent liquidity needs of Bear Stearns and forestall the potential systemic disruptions a default or bankruptcy of the company would cause in the already stressed credit markets, on Friday, March 14, 2008, the Board determined that unusual and exigent circumstances existed and authorized the FRBNY to extend credit to Bear Stearns through JPMC Bank. The purpose of the loan was to ensure that Bear Stearns would meet its obligations as they came due on Friday. This would allow for time during the weekend for Bear Stearns to explore options with other financial institutions that might enable it to avoid bankruptcy and for policy makers to continue to seek ways to contain the risk to financial markets in the event no private-sector solution proved possible.

On March 14, the FRBNY made an overnight discount window loan of $12.9 billion to JPMC Bank on a non-recourse basis and took as collateral assets of Bear Stearns with a value of $13.8 billion. The rate of interest on this loan was the rate for primary credit extended by the Reserve Banks, or 2.25 percent.[2] In a simultaneous back-to-back transaction, JPMC Bank provided secured financing to Bear Stearns and took as collateral the same assets that JPMC Bank used to secure its loan from the FRBNY. The FRBNY received no warrants or any other potential equity of either JPMC Bank or Bear Stearns in exchange for the loan.

On Monday morning, March 17, the $12.9 billion back-to-back loan through JPMC Bank to Bear Stearns was repaid in full to the FRBNY with interest of nearly $4 million. Thus, the loan resulted in a profit to the Federal Reserve and the taxpayers, and not in any loss to either.[3]

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[2] Section 10B of the Federal Reserve Act (12 U.S.C. § 347b) authorizes a Reserve Bank to make advances to depository institutions under certain conditions.

[3] On Sunday, March 16, 2008, in connection with the proposed acquisition of Bear Stearns by JPMorgan Chase & Co., the Board authorized the FRBNY under section 13(3) to extend credit to a limited liability company that would acquire assets from Bear Stearns where the credit would be secured exclusively by those assets. This extension of credit is the subject of a separate report being submitted under section 129 of the Emergency Economic Stabilization Act of 2008.

Report Pursuant to Section 129 of the Emergency Economic Stabilization Act of 2008: Loan To Facilitate the Acquisition of The Bear Stearns Companies, Inc. by JPMorgan Chase & Co.

Overview

On Sunday, March 16, 2008. the Board of Governors of the Federal Reserve System (Board), with the support of the Secretary of the Treasury and by unanimous vote of its five members, authorized under section 13(3) of the Federal Reserve Act (12 U.S.C. § 343) the Federal Reserve Bank of New York (FRBNY) to make a non-recourse loan to a limited liability company (Maiden Lane LLC ("Maiden Lane")) that would acquire $30 billion of identified, less liquid assets of The Bear Stearns Companies, Inc. (Bear Stearns). The loan would be repaid from the proceeds of the orderly disposition of these assets over time. The purpose of the loan was to facilitate the acquisition by JPMorgan Chase & Co. (JPMC) of Bear Stearns, which at the time was facing severe liquidity pressure that threatened to cause the default and bankruptcy of the company, with resulting risk to significantly stressed financial markets. The credit is secured by all of the assets acquired by Maiden Lane and by a subordinated loan of $1.1 billion from JPMC to Maiden Lane that would absorb any initial losses on the assets by that amount.

Background

In March 2008, Bear Stearns was one of the largest securities firms in the country. As of February 29, 2008, Bear Stearns reported total consolidated assets of approximately $399 billion. Bear Stearns engaged in a broad range of activities, including investment banking, securities and derivatives trading and clearing, brokerage services, and originating and securitizing commercial and residential mortgage loans. As a result of these activities, Bear Stearns maintained a large portfolio of mortgage-related securities and other debt instruments. Like most large securities firms, the company heavily financed itself in the short-term securities repurchase market.

Financial conditions deteriorated markedly between mid-January and mid-March 2008. Volatility was steadily increasing and liquidity was quickly declining in many credit markets – including in particular the market for residential mortgage-backed securities, but also in the markets for other asset-backed securities, corporate securities, and municipal securities. Moreover, many market participants were financing a large portion of their holdings of these long-term securities in short-term collateralized funding markets.

The senior management of Bear Stearns notified the Federal Reserve on the evening of Thursday, March 13, that it anticipated that many of its counterparties would on Friday not agree to roll over their repurchase agreements and, therefore, that Bear Stearns would be required on Friday to repay a significant portion of its repurchase agreement liabilities. Bear Stearns expected that it would not have sufficient funds or liquid assets to repay these obligations as they came due and would not be able during the short period before the markets opened on Friday to find a private-sector source of alternative financing. Bear Stearns reported that it would likely have to file for bankruptcy protection on Friday unless the Federal Reserve were willing to provide Bear Stearns with liquidity.

The sudden imminence of insolvency for Bear Stearns, the large presence of Bear Stearns in several important financial markets (including in particular the markets for repo-style transactions, over-the-counter derivative and foreign exchange transactions, mortgage-backed securities, and securities clearing services), and the potential for contagion to similarly situated firms raised significant concern that financial markets would be seriously disrupted if Bear Stearns were suddenly unable to meet its obligations to counterparties. Most crucially, the consequences of an unexpected and disorderly default or insolvency by Bear Stearns – a major borrower and lender in the repurchase agreement market – could have seriously disrupted this very large, important, and increasingly strained market for short-term secured financing. Market participants were likely to respond to the failure of Bear Stearns by withdrawing generally from short-term collateralized funding markets, resulting in a dramatic drop in the overall availability of short-term financing, and threats to the liquidity and possibly the solvency of other large and highly leveraged financial institutions.

To address the imminent liquidity needs of Bear Stearns and forestall the potential systemic disruptions a default or bankruptcy of the company would cause in the already stressed credit markets, on Friday, March 14, 2008, the Board determined that unusual and exigent circumstances existed and authorized the FRBNY to extend overnight credit to Bear Stearns through JPMorgan Chase Bank. The purpose of the loan was to ensure that Bear Stearns would meet its obligations as they came due on Friday. This would allow for time during the weekend for Bear Stearns to explore options with other financial institutions that might enable it to avoid bankruptcy and for policy makers to continue to seek ways to contain the risk to financial markets in the event no private-sector solution proved possible. The bridge loan provided on March 14, 2008, is the subject of a separate report being submitted under section 129 of the Emergency Economic Stabilization Act of 2008.

Despite the receipt by Bear Stearns of Federal Reserve funding on March 14, market pressures on Bear Stearns worsened throughout the day on March 14 and continued to worsen during the weekend. In light of the further erosion of confidence in Bear Stearns over the weekend by its chief short-term liquidity providers and capital markets transaction counterparties, Bear Stearns likely would have been unable to avoid bankruptcy on Monday, March 17, without either very large injections of liquidity from the Federal Reserve or an acquisition of Bear Stearns by a stronger firm.

During the period from March 13 through March 16, Bear Stearns actively sought both capital injections and acquisition partners. JPMC emerged as the only viable bidder for Bear Stearns on Sunday, March 16. Bear Stearns determined that only JPMC offered a credible proposal that would allow Bear Stearns to meet its obligations beginning Monday, March 17. Accordingly, on Sunday, March 16, Bear Stearns accepted the offer to merge with JPMC.

JPMC believed that it would be unable to acquire Bear Stearns, however, if it were required to obtain funding in the strained credit markets for a specified portfolio of less liquid assets of Bear Stearns. Bear Stearns itself was unable to secure adequate credit accommodations for those assets from private sources. Because no other funding source for these assets appeared available, emergency financing from the Federal Reserve with respect to those assets was necessary to facilitate JPMC's prompt acquisition of Bear Stearns, which would alleviate the intense strains in the credit

markets described above that were likely to result from the failure of Bear Stearns.

Terms of the Extension of Credit To Facilitate the Acquisition of Bear Stearns

On Sunday, March 16, 2008, the Board, finding unusual and exigent circumstances, authorized the FRBNY under section 13(3) to extend non-recourse credit of up to $30 billion to a limited liability company that would acquire a pool of assets of Bear Stearns in connection with the acquisition of Bear Stearns by JPMC. The credit would be repaid from the earnings on and the proceeds of the disposition of the assets in an orderly manner over time.

In the following weeks, the interested parties negotiated the details of these transactions and refined the terms. On March 24, 2008, the FRBNY and JPMC agreed to a Summary of Terms and Conditions that described the basic elements of the FRBNY's extension of credit. A copy of the Summary of Terms and Conditions is Attachment A to this report.

Pursuant to the summary of terms and conditions, a newly-formed limited liability company, Maiden Lane, would purchase $30 billion in assets from Bear Stearns on or about the date JPMC acquired Bear Stearns. The assets would be valued based on Bear Stearns' marks as of March 14, 2008. The assets purchased would have to meet each of the following parameters: (i) U.S. dollar denominated; (ii) U.S. domiciled; and (iii) performing residential and commercial mortgages or investment-grade or Agency issued securities (and related hedges). A performing mortgage is a mortgage that was no more than 30 days past due (as of March 14, 2008), and an investment-grade security is a security rated BBB- or higher by all rating agencies that have rated the security (as of March 14, 2008), including at least one of the three principal credit rating agencies. The FRBNY would retain an asset manager, BlackRock Financial Management, Inc. and its affiliates, to manage the assets of Maiden Lane.

To finance the purchase, the FRBNY would lend $29 billion to Maiden Lane. JPMC would make a $1 billion loan to Maiden Lane that would be subordinated in right of payment to the FRBNY's loan. Maiden Lane would be obligated to repay all of the principal and interest on the FRBNY's loan before making principal or interest payments on the JPMC loan. Any residual cash flows would be paid to the FRBNY. The FRBNY

would not receive any warrants or other equity interest in exchange for the loan in addition to the right to receive any residual cash flow. The FRBNY and JPMC loans would be secured by a first priority security interest in all of the assets of Maiden Lane.

Both loans would mature in ten years, subject to extension by the FRBNY. The FRBNY loan would earn interest at the rate for primary credit extended by FRBNY in effect from time to time. The loan by JPMC would earn interest at the primary credit rate in effect from time to time plus 450 basis points.[1]

On June 26, 2008, after all applicable regulatory approvals were obtained, JPMC's acquisition of Bear Stearns closed and the FRBNY and JPMC loans to Maiden Lane were closed in accordance with the provisions of the Summary of Terms and Conditions.[2]

Beginning after June 26, 2008, the Board's weekly H.4.1 Statistical Release, "Factors Affecting Reserve Balances of Depository Institutions and Condition Statement of the Federal Reserve Banks," includes information related to Maiden Lane. Among other things, the release discloses, as of the date of the release, the aggregate fair value of Maiden Lane's net portfolio holdings and the book value of the principal and interest on the loans made to facilitate the Bear Stearns acquisition. The fair value of the net portfolio holdings of Maiden Lane is updated quarterly to reflect values at the end of each calendar quarter. Consistent with generally accepted accounting principles, the assets and liabilities of Maiden Lane have been consolidated with the assets and liabilities of the FRBNY in the statements of conditions shown on the release because the FRBNY is the primary beneficiary of Maiden Lane. The H.4.1 release is published on Thursdays and is available on the Board's public website.

As noted above, the FRBNY loan will be repaid from the proceeds of the sale of the assets held by Maiden Lane, plus any earnings derived from

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[1] On June 26, 2008, when the loan transactions were executed, the primary credit rate was 2.00 percent.

[2] Because of adjustments in the values of some of the assets purchased by Maiden Lane from Bear Stearns, the amounts of the loans by FRBNY and JPMC were modified slightly from the values stated in the Summary of Terms and Conditions. The actual amount lent by the FRBNY was approximately $28.9 billion and the subordinated loan from JPMC was approximately $1.1 billion.

the assets prior to sale. The aggregate fair value of the Maiden Lane net portfolio holdings, which is updated quarterly to reflect values at the end of each calendar quarter, is reflected in the financial statements of the Federal Reserve Banks. Because the fair value reflects an estimated price that would be received if the assets were sold on the measurement date, the current fair value of the Maiden Lane holdings may fluctuate over different reporting periods. However, because the collateral assets for the loans are expected to be sold over time, the aggregate fair value for the Maiden Lane net portfolio holdings reported in any particular H.4.1 release does not reflect the amount of aggregate proceeds that could be received when the assets are actually sold over time.

A number of facts mitigate the risk of losses being incurred on the FRBNY loan. First, there is a substantial pool of professionally-managed collateral at Maiden Lane that, as of March 14, 2008, was valued at $30 billion. In addition, JPMC's subordinated loan to Maiden Lane will absorb the first $1.1 billion of any loss that ultimately occurs. Moreover, and perhaps most importantly, the collateral will be sold over time in an orderly manner that is not affected by the unnaturally strong downward market pressures that have been associated with the recent liquidity crisis. Finally, the FRBNY is entitled to any residual cash flow generated by the collateral after the FRBNY and JPMC loans are repaid. Given these protections, the Board at this time does not believe that the extension of credit to facilitate the acquisition of Bear Stearns will result in any net cost to the taxpayers resulting from the failure to repay the principal and interest of the FRBNY loan.

ATTACHMENT A